IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 120 and 276 both of 1985

For Approval and Signature:

Hon'ble CHIEF JUSTICE MR DM DHARMADHIKARI
and
Hon'ble MR.JUSTICE M.S.SHAH

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1. Whether Reporters of Local Papers may be allowed to see the judgements? : NO

2. To be referred to the Reporter or not? : NO

3. Whether Their Lordships wish to see the fair copy of the judgement? : NO

4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder? : NO

5. Whether it is to be circulated to the Civil Judge? : NO

PUNJALAL L. SHAH (HUF)

Versus

COMMISSIONER OF INCOME-TAX

Appearance:
MR JP SHAH for Petitioner
MR MANISH R BHATT for Respondent No. 1

CORAM : CHIEF JUSTICE MR DM DHARMADHIKARI
and
MR.JUSTICE M.S.SHAH

Date of decision: /12/2000

C.A.V. JUDGEMENT

(Per : CHIEF JUSTICE MR DM DHARMADHIKARI)

#. These Income Tax References Nos. 120 of 1985 and 276 of 1985 under Section 256(1) of the Income Tax Act, 1961 (for short `the Act') have been made to this Court seeking its opinion in the cases pertaining to assessment years 1980-81 and 1981-82 & 1982-83. On similar facts the following questions of law have been referred:-

ITR 120 OF 1985

"1. Whether on the facts and in the circumstances of the case, the entire share of profit of 32%, 30% and 39% in the firms of M/s. Pipe Dealers, M/s Tube Dealers and M/s. Pipe Distributors, was taxable in the hands of the assessee?

2. Whether on the facts and in the circumstances of the case, the enhancement of income made by the Commissioner (Appeals) was valid in law?"

ITR 276 OF 1985

"Whether, on the facts and in the circumstances of the case, the interest-income earned by the alleged smaller H.U.Fs was rightly included in the total income of the assessee-HUF?

#. The relevant facts giving rise to the aforesaid three questions are as under:-

The assessee is assessed in the year 1980-81 for previous year ending on 21-10-1979 to income tax in the status of Hindu Undivided Family (HUF). The HUF consisted of five members. The assessee HUF is a partner in three firms, viz. M/s. Pipe Dealers, M/s. Tube Dealers and M/s. Pipe Distributors, having 32%, 30% and 39% shares respectively. Three separate deeds of partial partition dated 29-9-1979, 3-10-1979 and 4-10-1979 were executed under which Shri Sharadkumar Pujalal Shah separated with 5% share in M/s. Pipe Dealers, Shri Atulkumar Pujalal Shah separated with 5% share from M/s. Tube Dealers and Shri Pujalal Lallubhai Shah separated with 4% share from M/s. Pipe Distributors. Consequent upon the above three partial partitions resulting in separation of three members of the HUF, deeds of partnerships were executed in respect of the aforesaid three firms on 3-10-1979, 5-10-1979 and 5-10-1979 respectively by incorporating the necessary changes consequent upon the partial partition of the HUF.

#. The HUF consisting four members filed returns declaring Rs. 29,150/- being 27% share from M/s. Pipe Dealers, Rs. 31,250 being 25% share from M/s. Tube Dealers and Rs. 45,679/- being 35% share from M/s. Pipe Distributors.

#. The Income Tax Officer framed assessments on protective basis and issued draft assessment order under Section 143(3)/144B of the Act. The assessee HUF took a stand before the Income Tax Officer that due to above mentioned partial partition, it has no longer remained a partner in any of the three firms and therefore, share of profit from each of the said three firms was not includible in its total income.

#. The Income Tax Officer rejected the contention of the assessee stating that in view of the provisions of subsection (9), inserted by amendment in Section 171, the partial partitions cannot be recognised and the HUF will be taxed in the same status as the partner of three partnership firms. Subsection (9) in Section 171 was inserted by the Finance (No.2) Act of 1980 with effect from 1-4-1980 and being directly relevant for answering the questions referred, is reproduced in full as under:-

"Notwithstanding anything contained in the foregoing provisions of this section, where a partial partition has taken place after the 31st day of December, 1978 among the members of a Hindu undivided family hitherto assessed as undivided, -

(a) no claim that such partial partition has taken place shall be inquired into under sub-section (2) and no finding shall be recorded under sub-section (3) that such partial partition had taken place and any finding recorded under sub-section (3) to that effect whether before or after the 18th day of June, 1980, being the date of introduction of the Finance (No. 2) Bill, 1980, shall be null and void;

(b) such family shall continue to be liable to be assessed under this Act, as if no such partial partition had taken place;

(c) each member or group of members of such family immediately before such partial partition and the family shall be jointly and severally liable for any tax, penalty, interest, fine or other sum payable under this Act by the family in respect of any period, whether before or after such partial partition.

(d) the several liability of any member or group of members aforesaid shall be computed according to the portion of the joint family property allotted to him or it at such partial partition,

and the provisions of this Act shall apply accordingly.

Explanation. - In this Section, -

(a) "partition" means -

(i) where the property admits of physical division, a physical division of the property, but a physical division of the income without a physical division of the property producing the income shall not be deemed to be a partition; or

(ii) where the property does not admit of a physical division, then such division as the property admits of, but a mere severance of status shall not be deemed to be a partition;

(b) "Partial partition" means a partition which is partial as regards the persons constituting the Hindu undivided family, or the properties belonging to the Hindu undivided family, or both."

#. As the opening part of the provision contained in Subsection (9) of Section 171 states any partial partition which has taken place after 31st day of December 1978 is unrecognisable and as per clause (b) of Subsection (9) the HUF shall continue to be liable to be assessed as if no such partial partition had taken place.

#. When the matter was taken by the assessee in Appeal, the Commissioner (Appeals) noticed that to give full effect to subsection (9) of Section 171 of the Act, the original share of profit, viz. 32%, 30% and 39% in the three above named firms respectively was liable to be brought to tax in the hands of the HUF and not 27%, 25% and 35% respectively, as was done by the assessing officer on the basis of separation of three members from the HUF leaving 27%, 25% and 35% share of profit of the remaining HUF.

#. The assessee HUF then preferred Appeal to the Tribunal. The Tribunal confirmed the opinion of the assessing office based on the effect of the provisions of subsection (9) of

Section 171 and also approved the action of Commissioner (Appeals) in bringing to tax the original share income to the extent of 32%, 30% and 39% in the three partnership firms.

#. It is on the above facts that the Tribunal has referred the above questions for the opinion of this Court.

##. Learned counsel Shri J.P. Shah appearing for the assessee mainly raised two contentions. Firstly, it is submitted that the Income Tax Law contained in subsection (9) of Section 171 of the Act cannot take away the right in accordance with Hindu Law of members of a HUF to effect a total or partial partition. After the partial partition, it is not the original bigger HUF but the smaller truncated HUF which continued to be partner in the three above mentioned firms. The share of profit or income of the smaller HUF in the partnership firms could not be taxed in the hands of the erstwhile bigger HUF. The second submission made on behalf of the assessee is that subsection (9) of Section 171 may not recognise the fact of partial partition having taken place after the appointed date 31-12-1978, but the there was no legal inhibition to hold that the smaller HUF had only remained as partner of the three firms and the assessing officer was, therefore, right in not bringing to tax the whole share of profit of the original HUF to the extent of 32%, 30% and 39% respectively in three firms but in including for tax only 27%, 25% and 35% respectively as a result of separation of three of the members of the HUF in partial partition and subsequent execution of fresh partnership deeds.

##. So far as the second question referred to this Court in ITR 120 of 1985 is concerned, learned counsel submitted that its answer is dependent upon the answer to the first question and he does wish to press the question on the power of Commissioner (Appeals) to make the enhancement of income and bring to tax the initial share of profits of the original HUF to the extent of 32%, 30% and 39% instead of 27%, 25% and 35% in the three firms respectively.

##. Shri Akil Kureshi, learned counsel appearing for the Revenue in his reply submitted that the contention advanced on behalf of the assessee, if accepted, would defeat the object and nullify the effect of the provisions contained in subsection (9) of Section 171 which were inserted only to curb the tendency of HUF of effecting colourable or sham partial partitions only as a device to evade tax and as part of their tax planning. On behalf of the Revenue, learned counsel submits that partial partition effected after 31-12-1978 are not recognisable for the purpose of

income tax and the tax Authorities were fully justified in treating the original HUF as continuing and bringing to tax its full share of profit in the firms in which it was partner. It is pointed out that the validity of subsection (9) of Section 171 has been upheld by the Supreme Court in Union of India and others vs. M.V. Valliappan and others 238 ITR 1027.

##. The provisions contained in subsection (9) of Section 171 as introduced by amendment to the Act and the question of its constitutionality came up for consideration before the Supreme Court in the case of Valliappan (supra). The Hindu Law recognises right of members of joint family to effect a partial or total partition. With a view to avoid or reduce the tax liability partial partitions in case of HUF assessee were found to be continuing in large scale resulting in adverse effect on the revenue. With that object in view subsection (9) was added to Section 171 giving a cut off date that any partial partition effected after 31-12-1979 will not be recognised and the HUF shall be continued to be liable to be assessed as if no partition has taken place in the family. In the case of Velliappan, while upholding the validity of subsection (9) of Section 171, the Supreme Court observed:

> "It is for the Legislature to recognise or not to recognise partial partition of the Hindu undivided family property for the purpose of levy and collection of tax, it is also for the Legislature to decide whether only non bona fide partial partition undertaken for reducing the tax liability should be recognised or not to recognise all partial partitions of the Hindu undivided family properties."

##. The Supreme Court further went on to observe:

> "Lastly, once the partial partition is not recognised, tax is to be calculated as if the assets are held by the Hindu undivided family. Hence, the question whether the Hindu undivided family is required to recover tax from the person to whom the properties are allotted, is not required to be considered by the taxing authority as for the purpose of income-tax the properties belong to the Hindu undivided family. If the Hindu undivided family finds any hardship, it is for the members of the Hindu undivided family to have the partition of the entire estate and not to have partial partition."

##. As has been held by the Supreme Court in Valliappan's case (supra), once the income tax law can validly refuse to recognise the partial partition in a Hindu undivided family, the liability of the erstwhile Hindu undivided family for assessment for payment of tax would continue to be the same as it existed before the partial partition. The argument advanced on behalf of the assessee cannot be accepted that although the partial partition is not recognisable, yet, in considering the share in the income of the partnership firm the smaller Hindu undivided family can be recognised for determining the tax liability.

##. As has been contended in reply on behalf of the Revenue, such argument on behalf of the assessee cannot be accepted as that would nullify the effect of the provisions contained in subsection (9) of Section 171 and would directly frustrate the very purpose of the amended provision, as in that case the partial partition would have to be recognised partly for the purpose of determining the share of income of the smaller Hindu undivided family in the three partnership firms. Once the law contained in subsection (9) of Section 171 prohibits recognition of any partial partition of Hindu undivided family, full effect to such prohibition has to be given in determining the tax liability of the so called erstwhile Hindu undivided family as existed prior to the partial partition. The argument, therefore, advanced on behalf of the assessee is unacceptable. We are supported in our conclusion by the earlier decisions of the Supreme Court in Kalloomal Tapeswari Prasad (HUF) v. Commissioner of Income-Tax, Kanpur (1982) 133 ITR 690 and the Andhra Pradesh High Court in the case of Commissioner of Income Tax v. S.V. Dalappa and Sons. (1989) 176 ITR 455 and Commissioner of Income-Tax v. Sri Krishna Motor and Engineering Works and others (1997) 228 ITR 347.

##. So far as the second question on the powers of the Commissioner of Appeals of enhancement of tax by treating the original share of profit to the extent of 32%, 30% and 39% in the three respective firms is concerned, as a result of the answer of the first question in favour of the Revenue, the said question has to be answered in favour of the Revenue. On the question of power of Commissioner to make enhancement, the learned counsel for the assessee rightly did not press the question in view of the clear provisions delineating scope of powers of the Commissioner under Sections 251(1)(a) in Appeal. He has been conferred with power to confirm, reduce, enhance or annul the assessment.

##. One question framed in Income Tax Reference No. 276 of 1985 on the taxability of the interest income earned by the Hindu undivided family, on answer of main question in favour of the Revenue, the said question also deserves to be answered in favour of the Revenue by holding that the interest income earned by the alleged smaller Hindu undivided family was rightly included in the total income of the original assessee (HUF).

##. In the aforesaid view of the matter, the two questions i.e, Question No. 1 and 2 in Income Tax Reference No. 120 of 1985 and the question framed in Income Tax Reference No. 276 of 1985 are answered in favour of the Revenue and against the assessee.

In the circumstances, we make no order as to costs.

(D.M. DHARMADHIKARI, C.J.)

(M.S. SHAH, J)

[sndevu]